

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition
of
Scallop Holding, Inc.

:

: AFFIDAVIT OF MAILING

for Redetermination of a Deficiency or Revision
of a Determination or Refund of Corporation
Franchise Tax under Article 9A of the Tax Law
for the Years 1978 - 1980.

:

:

State of New York :

ss.:

County of Albany :

David Parchuck, being duly sworn, deposes and says that he is an employee of the State Tax Commission, that he is over 18 years of age, and that on the 28th day of June, 1985, he served the within notice of decision by certified mail upon Scallop Holding, Inc., the petitioner in the within proceeding, by enclosing a true copy thereof in a securely sealed postpaid wrapper addressed as follows:

Scallop Holding, Inc.
One Rockefeller Plaza
New York, NY 10020

and by depositing same enclosed in a postpaid properly addressed wrapper in a post office under the exclusive care and custody of the United States Postal Service within the State of New York.

That deponent further says that the said addressee is the petitioner herein and that the address set forth on said wrapper is the last known address of the petitioner.

Sworn to before me this
28th day of June, 1985.

David Parchuck

James J. [Signature]
Authorized to administer oaths
pursuant to Tax Law section 174

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition :
of :
Scallop Holding, Inc. :

AFFIDAVIT OF MAILING

for Redetermination of a Deficiency or Revision :
of a Determination or Refund of Corporation :
Franchise Tax under Article 9A of the Tax Law :
for the Years 1978 - 1980.

State of New York :

ss.:

County of Albany :

David Parchuck, being duly sworn, deposes and says that he is an employee of the State Tax Commission, that he is over 18 years of age, and that on the 28th day of June, 1985, he served the within notice of decision by certified mail upon Philip L. Eiker, the representative of the petitioner in the within proceeding, by enclosing a true copy thereof in a securely sealed postpaid wrapper addressed as follows:

Philip L. Eiker
Scallop Holding, Inc.
One Rockefeller Plaza
New York, NY 10020

and by depositing same enclosed in a postpaid properly addressed wrapper in a post office under the exclusive care and custody of the United States Postal Service within the State of New York.

That deponent further says that the said addressee is the representative of the petitioner herein and that the address set forth on said wrapper is the last known address of the representative of the petitioner.

Sworn to before me this
28th day of June, 1985.

David Parchuck

James J. O'Day, Jr.
Authorized to administer oaths
pursuant to Tax Law section 174

STATE OF NEW YORK
STATE TAX COMMISSION
ALBANY, NEW YORK 12227

June 28, 1985

Scallop Holding, Inc.
One Rockefeller Plaza
New York, NY 10020

Gentlemen:

Please take notice of the decision of the State Tax Commission enclosed herewith.

You have now exhausted your right of review at the administrative level. Pursuant to section(s) 1090 of the Tax Law, a proceeding in court to review an adverse decision by the State Tax Commission may be instituted only under Article 78 of the Civil Practice Law and Rules, and must be commenced in the Supreme Court of the State of New York, Albany County, within 4 months from the date of this notice.

Inquiries concerning the computation of tax due or refund allowed in accordance with this decision may be addressed to:

NYS Dept. Taxation and Finance
Law Bureau - Litigation Unit
Building #9, State Campus
Albany, New York 12227
Phone # (518) 457-2070

Very truly yours,

STATE TAX COMMISSION

cc: Petitioner's Representative
Philip L. Eiker
Scallop Holding, Inc.
One Rockefeller Plaza
New York, NY 10020
Taxing Bureau's Representative

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition :
of :
SCALLOP HOLDING, INC. :
for Redetermination of a Deficiency or for :
Refund of Corporation Franchise Tax under :
Article 9-A of the Tax Law for the Years 1978 :
through 1980. :

Petitioner, Scallop Holding, Inc., One Rockefeller Plaza, New York, New York 10020, filed a petition for redetermination of a deficiency or for refund of corporation franchise tax under Article 9-A of the Tax Law for the years 1978 through 1980 (File No. 40223).

A formal hearing was held before Daniel J. Ranalli, Hearing Officer, at the offices of the State Tax Commission, Two World Trade Center, New York, New York, on December 4, 1984 at 1:15 P.M., with all briefs to be submitted by March 25, 1985. Petitioner appeared by John E. Meurling, Esq. and Robert J. Cestola, CPA. The Audit Division appeared by John P. Dugan, Esq. (Anna Colello, Esq., of counsel).

ISSUES

I. Whether interest on certain intercompany notes held by petitioner constituted investment capital within the meaning of section 208.5 of the Tax Law.

II. Whether, the interest, if held to be business capital, should be allocated within and without New York State.

FINDINGS OF FACT

1. Petitioner, Scallop Holding, Inc., filed New York State corporation franchise tax reports for the tax years 1978 through 1980. On its returns, petitioner treated certain intercompany loans to its affiliates, evidenced by promissory notes, as investment capital and interest received on these notes as investment income.

2. On August 31, 1982, as the result of a field audit, the Audit Division issued three notices of deficiency, pursuant to Article 9-A of the Tax Law, against petitioner as follows:

<u>Period Ended</u>	<u>Tax</u>	<u>Interest</u>	<u>Total Due</u>
12/31/78	\$127,834.00	\$49,060.00	\$176,894.00
12/31/79	\$281,443.00	\$84,090.00	\$365,533.00
12/31/80	\$379,916.00	\$81,218.00	\$461,134.00

3. Petitioner is a holding corporation owning 100 percent of the stock of five subsidiaries of which four do business in New York State. During the course of its business, petitioner made unsecured loans to three of its subsidiaries. These loans were evidenced by promissory notes. Petitioner's investment capital as reported on its returns consisted entirely of the three loans, along with United States treasury notes, Eurodollars (deposits with foreign banks) and cash.

4. On audit, the Audit Division reclassified the intercompany notes as business capital and the interest income as business income earned entirely within New York. The interest derived from the remaining investment capital was deemed to have an investment allocation of zero and was considered to be taxable at petitioner's business allocation of 100 percent.

5. Petitioner maintains that the intercompany loans are properly characterized as investment capital under the definition of investment capital in

section 208.5 of the Tax Law which includes "other securities" in the definition. Such a characterization would also allow petitioner's Eurodollars and treasury bills to be treated as investment capital. Petitioner submitted an opinion from a brokerage house to the effect that the promissory notes were not normally traded on securities exchanges but could be found in the high yield or private placement markets.

6. Alternatively, petitioner argues that, even if it has no investment capital, its short term investments in Eurodollars and treasury bills were made for the purpose of investing excess funds from subsidiaries which investments were not related to petitioner's business as a holding company. Thus, such income should be excluded from the receipts factor of the business allocation percentage since the income did not constitute business receipts.

7. Additionally, petitioner argues that the interest from intercompany loans should not be included in the business receipts factor to the extent that the income is derived from usage by the debtors outside of New York.

CONCLUSIONS OF LAW

A. That Tax Law section 208, subdivision 5, furnishes the definition of the term "investment capital" for purposes of Article 9-A as follows:

"The term 'investment capital' means investments in stocks, bonds and other securities, corporate and governmental, not held for sale to customers in the regular course of business, exclusive of subsidiary capital and stock issued by the taxpayer, provided, however, that, in the discretion of the tax commission, there shall be deducted from investment capital any liabilities payable by their terms on demand or within one year from the date incurred, other than loans or advances outstanding for more than a year as of any date during the year covered by the report, which are attributable to investment capital..."

Among the factors to be considered in determining whether these instruments were securities within the meaning of the above-quoted provision are the

following: (1) whether they are of the type customarily sold on the open market or on a recognized exchange; (2) whether they are designed as a means of investment; (3) whether they are commonly recognized by investors as securities; (4) whether they are issued for the purpose of financing corporate enterprises and providing a distribution of the rights in or obligations of such enterprises; and (5) whether, once issued, they are traded as investments. (20 NYCRR 3-4.2(a) and (d); Avon Products, Inc. v. State Tax Commission, 90 A.D.2d 393).

B. That there is nothing in the record to indicate that the notes in issue were traded on the open market. In fact, petitioner's own evidence indicates that such notes are not normally traded on securities exchanges. The fact that the notes could have been but never were traded on the private placement or high yield markets is insufficient to establish that the instruments were securities (Matter of Mobil International Finance Corporation, State Tax Commission, July 26, 1984).

C. That 20 NYCRR 3-4.2(d) provides:

"At the election of the taxpayer, cash on hand and cash on deposit may be treated on any report as investment capital or as business capital...Certificates of deposit are deemed to be cash. An election may not be made to treat part of such cash as investment capital and part as business capital. No election to treat cash as investment capital may be made where the taxpayer has no other investment capital."

Additionally, 20 NYCRR 4-8.1(d) and (e) provide:

"(d) In all cases when the investment allocation percentage is zero, interest received on bank accounts, on obligations of the United States and its instrumentalities and obligations of the State of New York, its political subdivisions and its instrumentalities is multiplied by the business allocation percentage.

(e) Where a taxpayer owns no securities other than obligations of the United States and its instrumentalities and obligations of New York State, its political subdivisions

and its instrumentalities, the taxpayer's investment allocation percentage is zero. The interest from such securities must be multiplied by the business allocation percentage."

D. That inasmuch as petitioner's notes are not investment capital, the remainder of its claimed investment capital, consisting of Eurodollars and treasury bills, may not be treated as such. Petitioner's investment allocation percentage is zero and the interest from its bank deposits and treasury bills must be multiplied by its business allocation of 100 percent.

E. That the business allocation percentage is computed by adding together a property factor, a receipts factor weighted as two, and a payroll factor and dividing the total by four. (Tax Law §210.3[a]). The numerator of the receipts factor includes other business receipts (other than from the sale of tangible personal property, the performance of services, or from rents and royalties) earned within New York State. (Tax Law §210.3[a][2][D]). Where the activities performed in order to establish and maintain a loan are performed within New York, the interest income derived from such loan is considered to be earned within New York. To determine whether the interest is attributable entirely to New York, consideration should be given to such activities as solicitation, investigation, negotiation, approval and administration. Inasmuch as petitioner's offices are located in New York and it has not shown that any of the aforementioned activities occurred anywhere other than New York, the interest from the loans was earned within New York and is properly includible in the business receipts factor. Additionally, the business of petitioner as a holding company involved the investing of excess funds of its subsidiaries in short-term investments, thus the interest income from the Eurodollars and treasury bills was also includible in the business receipts factor.


F. That the petition of Scallop Holding, Inc. is denied and the notices of deficiency issued August 31, 1982 are sustained.


Dated: Albany, New York

STATE TAX COMMISSION

JUN 28 1985


PRESIDENT


COMMISSIONER


COMMISSIONER